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No. 82-52

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

ARIZONA GOVERNING COMMITTEE FOR TAX DEFERRED ANNUITY AND DEFERRED COMPENSATION PLANS, STATE OF ARIZONA, *et al.*,
Petitioners,

v.

NATHALIE NORRIS, on behalf of herself and all others similarly situated,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AMERICAN COUNCIL OF LIFE INSURANCE AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Arizona established a voluntary deferred compensation plan, funded entirely by deductions from the employee's salary. The employer, the State of Arizona, makes no contributions. The plan includes a lump sum option. In addition, an employee may elect to receive his or her deferred compensation through a number of investment media, including a life annuity provided by a private, independent insurance company. The life annuity option provides equal value to men and women. Because the monthly annuity payments are calculated by using sex-specific mortality tables, women receive smaller periodic payments than similarly situated men.

The question presented is whether this plan violates Title VII of the Civil Rights Act of 1964.

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BRIEF OF AMERICAN COUNCIL OF LIFE INSURANCE AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

This brief is filed on behalf of the American Council of Life Insurance, as amicus curiae, in support of Petitioners. Consent from counsel for both sides has been filed with the Clerk of this Court.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Ninth Circuit is reported at 671 F.2d 330. A copy of the opinion is reproduced in the Appendix to the Petition. The opinion of the United States District Court for the District of Arizona is reported at 486 F. Supp. 645; it is set forth in the Appendix to the Petition.

JURISDICTION

The judgment below was entered on March 11, 1982. The Petition for Writ of Certiorari was granted on October 12, 1982. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Section 703(a)(1) of Title VII of the Civil Rights Act of 1964 provides, in pertinent part:

> It shall be an unlawful employment practice for an employer—
>
> (1) to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race, color, religion, sex, or national origin. . . .

42 U.S.C. § 2000e-2(a)(1).

INTEREST OF THE AMICUS

The American Council of Life Insurance ("Council") represents the interests of 555 member life insurance companies, including most of the major life insurers in the United States. Its members currently hold more than ninety-five

percent of the life insurance in force in legal reserve life insurance companies in the United States. In addition, member companies account for ninty-nine percent of the insured private pension plan business in the United States. (The Lincoln National Life Insurance Company, the private insurance company which offered the life annuity option at issue here, is a member of the Council.) Thus, the Council has a direct and immediate interest in insurance practices, in general, and in the sound administration of pension plans, in particular.

The pension industry is large and affects many individuals. At the end of 1980, 26.1 million Americans were covered by private pension plans administered by U.S. legal reserve life insurance companies. *See* American Council of Life Insurance, 1981 Pension Facts. Assets backing these plans reached $165.8 billion, an increase of 19 percent over the immediately preceding year. *Id.*

Virtually all insurance companies, including members of the Council, have historically used sex-specific actuarial tables in calculating benefits under defined contribution plans, to account for the well recognized fact that, as a class, women live longer than men. Therefore, the decision below prohibiting the use of such tables will directly affect the current and future business operations of all insurance companies. Indeed, such a judicially forced break with the past will revolutionize the insurance industry.

The Council is concerned about the continued viability of employee retirement plans. An internal study conducted by the Council estimates that a prohibition against using sex-specific actuarial tables could increase the costs of retirement plans by as much as two billion dollars per year. The Superintendent of Insurance of New York has estimated that a total of $1.9-$2.1 billion would be needed to equalize the results of using sex-specific tables in New York funded pensions plans after the date of this Court's decision in *Los Angeles Department of Water and Power v. Manhart,* 435 U.S. 702, enough possibly to bankrupt the system. Lewis, *Manhart et Sequentia: A 20 Billion Dollar Cost to Local Governments?,* 7 Employee Benefits J. 8, 13 (1982).

In any aspect of insurance, accurate risk classification is essential to maintaining the financial integrity of a finite fund subject to partial liquidation upon the occurrence of events such as death or disability which are unpredictable on an individual basis. An individual's sex, like age, provides an objective statistical basis for accurately assessing various risks presented by that individual. As a result of several lower court decisions, including the decision below, the insurance industry's traditional and historically-accepted practice of using sex-specific mortality tables has been cast into doubt. Because of its concern that employee retirement plans continue to be administered on a sound financial basis, the Council has a direct and immediate interest in the question presented.

STATEMENT

The Arizona Deferred Compensation Plan ("Plan") (Ariz. Rev. Stat. § § 38-871 *et seq.*) is a voluntary savings and investment plan established by the Arizona legislature to provide the approximately 35,000 state employees with an option to defer compensation and taxation on that income.[1] *Norris v. Arizona Governing Committee*, 486 F. Supp. 645, 648 (D. Ariz. 1980). The Plan is administered by the Arizona Governing Committee for Tax Deferred Annuity and Deferred Compensation Plans ("Governing Committee"), which is authorized by statute to contract with private, independent institutions for the purpose of establishing tax deferred compensation and annuity programs. *Id.* at 647. The Plan is offered strictly on a voluntary basis to all state employees and is funded entirely by employee contributions. *Id.* at 648.

Under the Plan, employees may, if they choose, have sums deducted from their pay and contributed to the Plan. During the "accumulation" phase of the Plan, employees are free to direct that their contributions be invested in a wide variety of

[1] The Arizona Deferred Compensation Plan is not a state operated retirement plan. The state retirement plan (Ariz. Rev. Stat. §§ 38-741 to-781.36, as amended) is entirely separate and provides for equal contributions and equal benefits.

funding media approved by the Governing Committee, including savings accounts, mutual funds, life insurance, or annuities. During the "pay-out" phase, the employee can elect to receive his or her deferred compensation in a variety of ways, e.g., (1) a lump sum payment, (2) a specific amount each month for a fixed number of months, or (3) a life annuity.

Respondent, Nathalie Norris, an employee of the State of Arizona, chose to participate in the Plan and to have her contributions invested in a life annuity to be provided by Lincoln National Life Insurance Co., one of the private, independent insurance companies designated by the Governing Committee. Although respondent made the preliminary choice of a life annuity, when she becomes eligible to receive her deferred income, she will have the option of receiving her accumulated compensation and earnings in a variety of ways, including (1) a lump sum, (2) a specific sum for a fixed number of months, or (3) a life annuity.

All insurance companies participating in the Plan, including Lincoln National, follow the long-established industry practice and use sex-specific mortality tables in calculating the periodic payments under a life annuity. Thus, because a woman has a statistical probability of living longer than a man, the annuity contracts provide that a woman will receive smaller monthly payments than a similarly situated man. The actuarial values of the annuity contracts are identical for men and women, and the average woman will receive more dollars than the average man because of the interest accruing to the woman over a longer period.

Respondent, after making her investment choice (a life annuity provided by Lincoln National), but before becoming eligible to receive her deferred compensation (at which time she will have the payment options described above), filed a class action in the United States District Court for the District of Arizona on behalf of herself and all female employees who have chosen, or will choose, to enroll in the Plan. Respondent contended that, because the private insurance companies designated by the Governing Committee use sex-specific mortality tables, the State of Arizona, the Governing Committee, and the

Committee's individual members violated Title VII and the equal protection clause of the Fourteenth Amendment.

Proceedings Below

The parties filed cross motions for summary judgment based upon stipulated facts. The district court found that, although the facts presented were different from those in *Manhart*, the broad reasoning of that decision required the same result, i.e., a finding of discrimination proscribed by Title VII.

The court concluded that the "open market" exception enunciated in *Manhart* was not applicable; the employees that chose to participate in the Plan were required to "select an option offered by one of the funding media approved by the State." 486 F. Supp. at 650. According to the court, the fact that employees could choose nondiscriminatory options, e.g., a lump sum distribution or a fixed annuity, had "no bearing on the lawfulness of the plan." *Id.* The court concluded: "the Deferred Compensation Plan of the State of Arizona, which provides or permits smaller monthly annuity payments to a female employee than to a male employee contributing the same amount, is discriminatory and in violation of Title VII of the 1964 Civil Rights Act." *Id.* at 652.

With respect to the equal protection claim, however, the court found that because petitioners did not have the intent to discriminate, no constitutional violation had been established. "From the facts agreed upon, it . . . [was] clear that [the challenged] classification was not made by the defendants but rather . . . [was] the result[ ] of the insurers' judgment." 486 F. Supp. at 651.

After certifying the suit as a class action, the court permanently enjoined petitioners from carrying out their obligations under the Plan through the use of sex-specific mortality tables, and ordered that the State of Arizona ensure that monthly annuity payments to female retirees be equal to payments to similarly situated males.

The court of appeals affirmed in a two to one decision, District Judge Nielson dissenting. Rejecting the careful limitations this Court placed on its holding in *Manhart* in favor of an expansive application of its reasoning, the Ninth Circuit refused to distinguish the Arizona Plan. In *Manhart*, which involved an employer-operated plan, this Court carefully noted that "[n]o private insurance company is involved in the administration or payment of benefits," 435 U.S. at 705, and that "Title VII . . . primarily govern[s] relations between employees and their employers, not between employees and third parties." 435 U.S. at 718 n.33. Referring to a footnote in *Manhart* which stated that Title VII applies to "any agent" of a covered employer and that an employer could not avoid responsibility by delegating discriminatory programs to a corporate shell, 435 U.S. at 718 n.33, the court of appeals asserted that, because the State had selected the companies which offered the discriminatory plans, *Manhart* was controlling. 671 F.2d at 334.

The court of appeals also rejected the applicability of *Manhart's* "open market" exception. In *Manhart*, this Court had stated: "Nothing in our holding implies that it would be unlawful for an employer to set aside equal retirement contributions for each employee and let each retiree purchase the largest benefit which his or her accumulated contributions could command in the open market." 435 U.S. at 717-18 (footnote omitted). Although it recognized that the lump sum option in the Arizona Plan could not be considered discriminatory, the court of appeals found that, because Arizona had done more than offer nondiscriminatory options, it could not take refuge in the "open market" exception. And, even though the Arizona Plan simply reflected the limits in the marketplace, the defendants had run afoul of Title VII by "affirmatively offer[ing] a plan . . . which discriminated against women." 671 F.2d at 335.

The court of appeals rejected the argument that the McCarran-Ferguson Act (15 U.S.C. §§ 1011 *et seq.*) prohibited the application of Title VII. Because no insurance company was a party to the suit, the court concluded that "the district court has not interfered with the business of insurance." 671 F.2d at 333.

The court disposed of defendants' contention that Title VII required an intent to discriminate in a disparate treatment case by reading *Manhart* as not requiring an affirmative showing of intent. "Nowhere [in *Manhart*] was the need to prove intent discussed." 671 F.2d at 333. Moreover, according to the court, "because on their face the practices in question treat men and women differently, Norris . . . [was] not [required to] prove Arizona's animus in adopting the plan." *Id.* at 334.

In his dissent, Judge Nielson concluded "that Arizona's voluntary Deferred Compensation Plan falls clearly within the *Manhart* open market exception." 671 F.2d at 336.

SUMMARY OF ARGUMENT

It is not disputed in this case that women, as a class, live longer than men. Sex-specific mortality tables recognize the fact that a person's sex has a demonstrable statistical relationship to longevity. The use of such tables enables an insurance company to make a more accurate assessment of an individual's life expectancy than would otherwise be possible. The tables also allow an insurance company to provide annuity plans of equal value for persons of each sex. Because an individual woman has a greater life expectancy than a similarly situated man, an annuity plan of identical actuarial value will provide smaller periodic payments to a woman than to a man.

The size of the periodic payment is not, however, the proper measure of whether an annuitant has been treated fairly. The product purchased by an annuitant is the *promise* to pay the specified amounts *if* the annuitant survives to collect. On the date of purchase, the *present value* of a policy purchased by a woman will be *equal* to the value of a policy purchased by a similarly situated man. There is, therefore, equality of treatment consistent with Title VII.

As the decision of the Sixth Circuit in *Peters* shows, this Court's decision in *Manhart* is not controlling when an annuity plan operated by a third-party insurer provides benefits of

equal value for equal contributions. *Manhart* involved an employer-operated plan requiring women to make larger contributions than men. The Arizona Deferred Compensation Plan is not employer-operated; independent insurance companies manage the funds and calculate the benefits. The employer makes no contributions and there is no requirement that male and female participants make unequal contributions. And, because the Arizona Plan provides men and women with benefits of equal value for equal contributions, there is equality of treatment consistent with Title VII.

Although explicit sex classifications are generally invalid, Title VII does not set forth a per se rule of illegality. Although there are no exceptions to the statutory rule against racial classifications, distinctions between the sexes can be drawn when there are strong efficiency interests at stake or when there is a broadly shared social norm that permits differences in treatment. Here, because there is a demonstrable statistical relationship between a person's sex and longevity, there are strong justifications for such a classification. Alternative criteria are not easily available, and the recognition that women live longer than men is not based on an archaic stereotype about the appropriate role of women in society. Use of the long recognized factual relationship between sex and life expectancy does not result in discrimination on the basis of sex proscribed by Title VII.

A prohibition on the use of sex-specific mortality tables would have a number of adverse consequences. The failure to consider a woman's longer life expectancy would result in her receiving greater value than a similarly situated man. There is a risk that the increased costs associated with providing equal annuity payments to women might provide employers with an incentive to discriminate against women. If a pension plan does not take account of lower male life expectancy, men will have an incentive to opt out in order to obtain better benefits from an insurance company which does use sex-specific mortality tables. A "unisex" plan would be inherently unstable and subject to adverse selection.

The Arizona Plan satisfies *Manhart's* "open market" exception. The Plan is entirely voluntary and provides concededly nondiscriminatory benefits which enable participants to purchase the largest benefit available on the open market. Moreover, the Plan simply makes available a range of options which exist in the marketplace. As the district court found, petitioners exhibited no intent to discriminate; the challenged classification was the result of the insurers' judgment. And, if life annuities were to be offered they would have to be provided by an insurance company which uses sex-specific mortality tables. The Council is not aware of any private insurance company which offers an annuity plan which does not calculate benefits according to sex-specific mortality tables. The most likely consequence of prohibiting the use of such tables will be to eliminate life annuities as a deferred compensation option.

ARGUMENT

I. There is Equality of Treatment Consistent with Title VII When a Voluntary Deferred Compensation Plan Provides Benefits of Equal Value for Equal Contributions.

A. The Use of Sex-Specific Mortality Tables Allows an Insurance Company to Provide Men and Women with Annuity Plans of Equal Value for Equal Contributions.

Insurance exists for the purpose of risk-sharing. Certain events, such as death, disability, or fire, are not predictable with certainty. If individuals could predict these events with precision, they could plan accordingly, though they might not be able to provide sufficient funds to cover the event. But since, for example, the date of a person's death is not predictable in any absolute sense, people are willing to pay a price to transfer the risk to another. When an insurance policy is purchased, the risk is assumed by the insurer, who pays in accordance with the outcome of the risk.

The insurer then must undertake—or "underwrite"—the burden of assessing the probability that the event insured against will occur, within specific times. Accordingly, accurate risk assessment is essential to maintaining the financial solvency

of a finite fund which is subject to partial liquidation on the occurrence of events which are not predictable in any absolute sense on an individual basis.

In assessing the probability that a hazard depending on life contingencies will occur, the insurer will necessarily examine the experience of a large number of individuals who, because of certain relevant characteristics, present similar risks. The selection of the individual characteristics which will be considered is not arbitrary. An insurer will only decide to consider characteristics when the available data and the insurer's experience establish that a characteristic has a demonstrable statistical relationship to the risk in question. This is the essence of the art of underwriting.

An insurer will not, however, take into account every individual characteristic which has *any* relationship to the risk in question. The relationship between the characteristic and the risk must be stable and predictable. In addition, the predictive value gained by considering the characteristic must outweigh the costs of assessing whether the characteristic does in fact exist.

In dealing with annuities, an insurance company, if it is to remain solvent, must have some way of estimating the number of periodic payments it expects to make to an individual. The experience of insurance companies and the available actuarial data show that the two most stable, significant, and objectively measurable factors in predicting longevity are the age and sex of the annuitant.[2] Consideration of these two factors enables an

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[2] In *Peters v. Wayne State University*, 476 F. Supp. 1343, 1345 n.2 (E.D. Mich. 1979), the plaintiffs contended that other life expectancy predictors, such as health, weight, smoking, etc., could be used in computing annuity rates. However, the court found that "[t]he evidence . . . demonstrated that only the immutable factors of age and sex could be used." 476 F. Supp. at 1345 n.2.

Insurers do, of course, utilize these other factors in assessing the risk of individual *life insurance* applicants, and "select risk" policies for non-smokers, non-drinkers, etc., are commonplace in the insurance market. Even in the annuity market, where these other factors have an opposite effect on insurer liability (i.e., the good health risk would be expected to live longer

(footnote continues)

insurance company to assess accurately and efficiently the risks that that individual presents.

Sex-specific mortality tables enable an insurance company to make a more accurate assessment of an individual's life expectancy than it otherwise would be able to make.[3] The use of such tables allows an insurance company to provide annuity

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(footnote continued)

than average, and increase the annuity risk) insurers have in recent years marketed annuities to persons with severe health problems on a "substandard", or reduced rate, basis. These are frequently utilized in structured settlement cases involving personal injury and workers' compensation claims. However, in the broad market for individual annuities it would not be economical to establish multiple rating classes for annuities in view of the paucity of interest among unhealthy individuals. For example, the person in poor health can assure an adequate return by taking an annuity with payments guaranteed for a stated number of years.

[3] The suggestion is sometimes made that the insurance industry's decision to use mortality tables which group individuals according to their sex is arbitrary, random, or biased. The suggestion that the use of sex-specific mortality tables is done with the intent to disadvantage women is, however, simply incorrect. Insurance companies use sex-specific mortality tables because they make it possible to make a much more accurate assessment of an individual's life expectancy than would otherwise be possible.

Both current industry practice and historical experience attest to the fact that sex-specific mortality tables are used because of actuarial considerations. For example, the use of sex-specific mortality tables results in women paying *smaller* life insurance premiums than similarly situated men. And, life insurance premiums account for a much larger percentage of the insurance business than do annuity considerations. In 1981, life insurance premiums paid to American life insurance companies were $47.4 billion, compared with $28.6 billion for annuity considerations. American Council of Life Insurance, 1982 Life Insurance Fact Book. The historical record also dispels any suggestion that the use of sex-specific mortality tables is a means to disadvantage women. Over the last 200 years,

> life insurance premiums for women rose and fell in accord with the most recent study comparing male and female mortality. The availability and cost of disability insurance underwent similar variations. However, despite the early uncertainty surrounding this classification, there can be little question anymore that classifying on the basis of the sex of the insured is statistically justified.

Bailey, Hutchison, and Narber, *The Regulatory Challenge To Life Insurance Classification*, 25 Drake L. Rev. 779, 786 (1976)(footnotes omitted). Of course, in this case respondent did not challenge the accuracy of sex-specific mortality tables.

plans of equal actuarial value. And, since an individual woman has a statistical probability of living longer than a similarly situated man, an annuity plan of identical actuarial value will promise smaller periodic payments to a woman than to a man.[4]

In determining whether men and women annuitants have been treated equally, however, the *periodic* payments that will ultimately be received are irrelevant. In deciding whether there has been unfair discrimination, it is necessary to focus on the product purchased by the insured. The proper focus is on the contractual rights received in exchange for the price of the annuity.[5] The purchaser of a policy does not buy the amounts that will be paid upon occurrence of the event insured against; rather, the product purchased is "the *promise* that *if* the event

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[4] Some have argued that a woman's longer life expectancy should not be considered because in a group of retirees of the same age with the same number of men and women it would be possible to match 84% of the men and women as to year of death. According to this "overlap" argument, it is unfair to treat all women differently because only a minority, i.e., 16%, live longer. The numerous critiques of this theory have shown its fallacies. *See, e.g.*, Benston, *supra*, at 515 n.72 (discussing the theory and citing the relevant literature); Kimball, *supra*, at 120-23. Although there are a number of reasons for rejecting the "overlap" theory, perhaps the most compelling is that the theory does not focus on the reason insurance companies use mortality tables, *viz.*, to obtain an accurate prediction of an individual's life expectancy. As Professor Benston states: "[A]n overlap of two distributions is irrelevant for assessing probabilities . . . ." Benston, *supra*, at 515 n.72. The same "overlap" argument can be made with respect to age; yet, no one seriously argues that age is not a relevant factor in predicting life expectancy. *See* Myers, *Forum: Pension Benefits and Sex*, 9 Civ. Rts. Dig. 45, 46 (1977).

[5] Thus, an insured who dies after receiving only one monthly payment has received the same value as an insured who lives for twenty years. As Justice Holmes stated in considering whether, for estate tax purposes, a life estate was to be valued on the basis of life expectancy on the date of the decedent's death or on the basis of the life tenant's actual longevity when the life tenant died before the estate tax was calculated:

> [T]he value of the thing to be taxed must be estimated as of the time when the act is done. But the value of property at a given time depends upon the relative intensity of the social desire for it at that time, expressed in the money that it would bring in the market. . . . Like all values, as the word is used by the law, it depends largely on more or less certain prophecies of the future; and the value is no less real at that time if later the prophecy turns out false than when it comes out true.

Ithaca Trust Co. v. United States, 279 U.S. 151, 155 (citation omitted).

occurs, the designated amount will be paid." Benston, *The Economics of Gender Discrimination in Employee Fringe Benefits: Manhart Revisited*, 49 U. Chi. L. Rev. 489, 497 (1982) (emphasis in original); *see* Kimball, *Reverse Sex Discrimination: Manhart*, 1979 Am. Bar Found. Research J. 83, 99-102. The value of the promise received in exchange for the price of the annuity policy "is measured by the present value of the amounts promised multiplied by the probability that the event insured against will occur. . . ." Benston, 49 U. Chi. L. Rev. at 503. At retirement, the present value of an annuity purchased by a woman is *identical* to the value of an annuity purchased by a similarly situated man.[6] Since the annuity plans offered to men and women are of identical value, there is equality of treatment consistent with Title VII.

B. As the Decision of the Sixth Circuit in *Peters v. Wayne State University* Shows, *Manhart* is Inapplicable to an Annuity Plan Operated by a Third-Party Insurer Which Provides Benefits of Equal Value for Equal Contributions.

Recently, the Sixth Circuit, in *Peters v. Wayne State University*, Nos. 79-1658,—1670,—1671 (decided Oct. 14,

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[6] Although at retirement the present values are identical, a woman annuitant who lives to the predicted age will receive greater total payments than a man who lives to the predicted age. Suppose a man and a woman both retire at age 65 with equal accumulations. Let X = the monthly income payments for the man, and Y = the monthly income payments for the woman. At the annuity starting date, the present values, including interest and mortality, of the periodic payments expected to be made during the lifetime of both the man and the woman are equal and are also equal to the accumulation. Let A = the number of months which is the average expected remaining lifetime (life expectancy) of the man, and B = the number of months which is the average expected remaining lifetime (life expectancy) of the woman. The "aggregate sum" of payments is equal to the total dollar amount, without interest, of periodic payments to be made assuming that each annuitant dies at the end of the average expected remaining lifetime. This is equal to AX for the man and BY for the woman. As shown by the table set forth in the Appendix to this brief, BY, the aggregate sum received by the woman, is in fact significantly greater than AX, the aggregate sum received by the man.

This could, indeed, be argued to be discrimination in favor of women, but that, of course, is not the case.

1982), *petition for cert. filed* (No. 82-794), analyzed a Title VII claim similar to the allegation presented by the respondent in this case. Wayne State offered its faculty and certain employees a pension plan administered by Teachers Insurance and Annuity Association and College Retirement Equities Fund (TIAA-CREF). Under the TIAA-CREF plan, which uses sex-specific mortality tables to calculate benefits, female annuitants receive smaller monthly payments than similarly situated males. The district court found that Wayne State, TIAA, and CREF had all violated Title VII. *Peters v. Wayne State University*, 476 F. Supp. 1343 (E.D. Mich. 1979). In a unanimous opinion, the court of appeals reversed.

The Sixth Circuit rejected the argument that this Court's holding in *Manhart* was dispositive. The court correctly noted that *Manhart* held only that an employer-operated pension fund requiring women to make *larger* contributions than men violated Title VII. As the Sixth Circuit observed, under the pension plan involved in *Manhart*, women received smaller take home pay than similarly situated men. In contrast, under the annuity plan offered at Wayne State, men and women made equal contributions. Also, unlike the situation in *Manhart*, the pension plan was not employer-operated; an independent insurer managed the fund and calculated the benefits.

Although it recognized that female annuitants receive smaller periodic payments when sex-specific mortality tables are used, the Sixth Circuit focused on the fact that "the present actuarial values of women's and men's benefits are identical," *Peters*, slip op. at 3, and concluded that "[c]areful analysis of Wayne State's actions reveals neither disparate treatment nor disparate impact." *Id.* at 5. The plaintiffs had not established that the recognition that every individual woman has the same statistical probability of outliving a man of the same age was "a pretext to mask . . . [an] intention to disadvantage and harm female annuitants." *Id.* at 7. Moreover, there was no adverse effect on women because "[t]he retirement plan [was] not worth more to men than to women." *Id.* at 9.

The Sixth Circuit found that the use of sex-specific mortality tables to calculate annuity benefits did not constitute discrimination *against* women. The court concluded:

> Common sense supports this holding. Plaintiffs point out that individual women may not live to the predicted statistical age of death and, therefore, may not recover the full actuarial value of their retirement packages. This argument is equally true for men. After death the total benefits received could be calculated to determine whether a man or a woman has received more money. But because annuity payments must be calculated prior to death, insurers and employers must use the only tools available to calculate payments, mortality tables. Both women and men may not live to the predicted statistical age but both women and men have the same probability of living to the predicted statistical age.
>
> * * *
>
> We conclude that Wayne State has not violated Title VII by providing women and men equal retirement annuity benefits with different disbursement rates.

Peters, slip op. at 9-10 (emphasis omitted).

The court in *Peters* recognized that not every difference in treatment amounts to discrimination, as defined by Title VII. The legality of the challenged practices can be determined only after a careful assessment of the reasons behind them and their overall operation, and not by focusing exclusively on a single payment among many.

The Sixth Circuit's decision in *Peters* shows that *Manhart* is inapplicable to the specific facts presented by the instant case. Like the Wayne State plan at issue in *Peters*, the Arizona Plan is not employer-operated; an independent insurance company manages the funds and calculates the benefits. In addition, unlike the situation in *Manhart*, the employer makes no contributions under the Arizona Plan. In fact, the employer is prohibited from so doing by state law. Also, unlike *Manhart*, the retirement plans in *Peters* and in the instant case did not

require male and female participants to pay unequal contributions. And, because the plans provide men and women with benefits of equal value for equal contributions, there is equality of treatment consistent with Title VII.

C. There is No Discrimination in Violation of Title VII When an Insurer Considers the Differences in Life Expectancy between the Sexes in Calculating Annuity Payments.

Respondent's Title VII allegation appears to be based on the simplistic notion that it is impermissible to resort to a characteristic mentioned by Title VII, even if that characteristic has a demonstrable statistical relationship to longevity. The argument for what appears to be a per se rule is, however, inconsistent with both the statutory framework and the case law. Although Title VII sets forth a rule of per se illegality for explicit racial distinctions, no such rule pertains in the area of sex discrimination. It appears "that although explicit sex classifications are presumptively invalid, they can be justified where there are strong efficiency interests at stake or where there is a broadly shared social norm that requires that men and women be treated differently." Freed and Polsby, *Privacy, Efficiency, and the Equality of Men and Women: A Revisionist View of Sex Discrimination in Employment,* 1981 Am. Bar Found. Research J. 585, 589.

Title VII recognizes that, in certain circumstances, it is permissible to consider sex in making employment-related decisions. For example, Section 703(e) allows an employer to base a hiring decision on the sex of an applicant "where . . . sex . . . is a bona fide occupational qualification reasonably necessary to the normal operation of that particular business or enterprise." 42 U.S.C. § 2000e-2(e). In addition, employers have been allowed to consider the sex of an employee because of "privacy" concerns, *e.g., Fesel v. Masonic Home,* 447 F. Supp. 1346 (D. Del. 1978), *aff'd,* 591 F.2d 1334 (3d Cir. 1979), or because of differences in dress or grooming standards. *E.g., Willingham v. Macon Telegraph Publishing Co.,* 507 F.2d 1084 (5th Cir. 1975) (en banc), *vacating* 482 F.2d 535 (5th Cir. 1973). Both Congress and the courts have recognized that

in limited situations, it is permissible to consider an employee's sex, when it would not be permissible to consider an employee's race.

The courts have suggested that employers may take into account differences between men and women when there is a strong correlation between sex and the characteristic in question. *See, e.g., Dothard v. Rawlinson,* 433 U.S. 321, 332-37; *Phillips v. Martin Marietta Corp.,* 400 U.S. 542 (per curiam). This exception is certainly not very broad.[7] For example, it would undoubtedly be impermissible to base an employment-related decision on a characteristic related to an employee's sex if an alternative criterion was easily available. Also, it would undoubtedly be impermissible to base an employment-related decision on a characteristic related to sex if to do so served to reinforce a stereotype as to the appropriate role of women in society.

In this context, taking into consideration a characteristic, i.e., life expectancy, which is related to sex does not run afoul of any of the limiting principles outlined above. Clearly, alternative criteria are not easily available.[8] "As . . . the voluminous

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[7] There is, of course, a danger that the claim that an employer is simply taking into account allegedly legitimate differences between the sexes may be a pretext for invidious discrimination. An employer might be indulging a taste for discrimination. Therefore, it would be necessary to require a strong empirical showing that there was indeed a demonstrable statistical relationship between sex and the characteristic in question.

Here, however, the stipulation entered into by the parties accepted the accuracy of sex-specific mortality tables. Some commentators have argued that "sex turns out to be a spurious, weak, and unstable predictor of mortality." Brilmayer, Hekeler, Laycock and Sullivan, *Sex Discrimination in Employer-Sponsored Insurance Plans: A Legal and Demographic Analysis,* 47 U. Chi. L. Rev. 505, 559 (1980). This conclusion has been subject to severe criticism. *See* Benston, *supra,* at 525-29. In any event, the demographic conclusions of the Brilmayer article are irrelevant in this case, since the parties have stipulated to the contrary.

[8] In contrast, the use of sex to predict weight-lifting ability would be impermissible in part because the employer has the option of administering an individual weight-lifting test which is highly predictive and cheap to administer. *See* Freed and Polsby, *supra,* at 628. An insurer who ignored a woman's longer life expectancy, however, "would incur substantial costs if it

(footnote continues)

actuarial science literature show[s], knowledge of an annuitant's gender permits a much more accurate assessment of the risk of that person's death than is provided by models that omit this variable." Benston, *supra*, at 524. And, to recognize that there is a demonstrable statistical relationship between sex and life expectancy does not perpetuate archaic and overbroad stereotypes about the appropriate role of women in society. Therefore, because "there is considerable evidence that a person's gender is a valid and useful predictor of that person's life expectancy," Benston, *supra*, at 542, i.e., there are strong efficiency justifications, and because alternative criteria are not easily available, making use of the relationship between sex and life expectancy does not result in discrimination on the basis of sex proscribed by Title VII.

D. A Prohibition on the Use of Sex-Specific Mortality Tables Would Result in Inequitable Treatment of Individuals and Serious Market Disruptions.

Using sex-specific mortality tables in calculating annuity payments enables insurers to give men and women equal value for equal contributions. In addition, the use of such tables enables insurers to operate retirement plans on a financially sound basis. In contrast, prohibiting the use of a characteristic which has a demonstrable statistical relationship to longevity will result in inequitable treatment of individuals and serious market disruptions. *See* Benston, *supra*, at 532-42.

First, the failure to take into account longer life expectancy will provide greater value to women. If a man and a woman acquire the right to receive equal monthly payments for life, there is no doubt that the *value* of the woman's *right* to the

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(footnote continued)

awaited an individualized determination of lifespan in the form of the insured person's death." *Id.* at 629. Because insurance requires that some estimates of future events be made, so that a sufficient fund can be established, this approach is not possible. "[O]nce the special characteristics of insurance are recognized for what they are, it is difficult to understand how it could be seriously maintained that individualized determinations of longevity are functionally similar to individualized determinations of weight-lifting ability. The logic of that argument, indeed, would apply to insurance in general." *Id.*

annuity is greater than the value of what a man of the same age would receive.[9]

Second, since there would be increased costs associated with providing equal annuity payments to women, there is a risk that employers might have an incentive to discriminate against women — a result directly in conflict with the Civil Rights Act.[10]

Third, men who either are participants or are eligible to participate in a pension plan which provides annuities on a basis which does not reflect the differences in life expectancy between men and women will, if they can, opt out in order to obtain better benefits from an insurance company which prices products using sex-specific mortality tables.[11]

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[9] This fact is illustrated by the tax laws which utilize sex-specific mortality tables in computing the "fair market value" of annuities. *See* I.R.C. §§ 170, 403, 691; Treas. Reg. §§ 172.9, 20.2031-10, 25.2512-9. Under the Arizona Plan the insurer is obligated to repay the accumulated value of each employee's account. If the employer currently pays an additional amount into a female's account to equalize periodic benefits in accordance with the district court's order, the accumulated value of the female's account will be greater than the male's. Upon retiring, female employees may then elect the lump sum option and immediately realize the increased value of their accounts. This is clear discrimination in favor of women. As this Court noted in *General Electric Co. v. Gilbert,* 429 U.S. 125, 139 n.17, the cost to insure against the risks in an employee benefit plan is, "in essence, nothing more than extra compensation to the employees, in the form of fringe benefits." Thus, the district court's order requiring Arizona to pay the added costs to equalize periodic benefits may well violate the Equal Pay Act of 1963, 29 U.S.C. § 206(d). By selecting the lump sum option, a woman would immediately realize the greater value of her account and receive greater total remuneration for services rendered than a similarly situated male. Even if she takes the annuity, she receives greater value for her services than the male.

[10] "Whether [the employer] apportions the contributions equally among all employees or actually contributes more for his female employees makes no difference; he knows that his pension costs are higher because he employs women. Thus, he has a powerful disincentive to hiring women, which will obviously 'tend to deprive' them of employment opportunities in violation of the statute." Bernstein & Williams, *Sex Discrimination in Pensions: Manhart's Holding v. Manhart's Dictum,* 78 Colum. L. Rev. 1241, 1243 (1978).

[11] The destructive effects of adverse selection in insurance have been historically documented. *See* Bailey, Hutchison, and Narber, *The Regulatory Challenge to Life Insurance Classification,* 25 Drake L. Rev. 779, 784-85 (1976).

Fourth, a "unisex" mortality table would not be a panacea. A pronouncement from the judiciary cannot change reality, and the reality, in this context, is that an individual woman has a greater probability of living longer than a similarly situated man. "Manifestly, an insurance company cannot disregard [the] fact [that women live longer then men]. . . ." *Equal Employment Opportunity Commission v. Colby College*, 589 F.2d 1139, 1144 (1st Cir. 1978) (Aldrich, J.). In *Manhart*, this Court stated that its holding did not "call into question the insurance industry practice of considering the composition of an employer's work force in determining the probable cost of a retirement or death benefit plan." 435 U.S. at 718 (footnote omitted). An insurance company, in devising a "unisex" table, would necessarily be required to consider the male-female composition of the work force covered by the plan. Of course, because the "mix" would be constantly changing, the "unisex" tables would be inherently unstable.[12] And, because a plan using a "unisex" table would undercompensate men and overcompensate women, the plan would be subject to adverse selection. Kimball, *supra*, at 133-35. As one author has concluded: "If *Manhart* is extended, the result not only will be unfair discrimination against individuals because of gender, but the potential destruction of annuities and life insurance, as the inexorable effects of adverse selection work their havoc." Benston, *supra*, at 542.

If the Arizona Plan is held to violate Title VII, life annuities could only be offered by using some sort of "unisex" mortality table. Such a table would provide lower periodic payments than those now established for men, but higher

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[12] The inherent instability of a unisex plan would have the greatest impact on employers with a small workforce.

> Companies with relatively few employees probably could not use a trusteed plan because random fluctuations in their actual experience could "break the bank." Hence, they would either have to use an insurance company (if there were any that would still write annuities under a mandated unisex mortality table), not offer nonvested retirement benefits, and/or attempt to employ fewer females.

Benston, *supra*, at 540.

periodic payments than those now provided women. Thus, a woman who elected a life annuity at the unisex rates would receive a larger monthly payment than would be the case if sex-specific mortality tables were used. However, men have a free election under the Arizona Plan. They would not voluntarily choose annuities based on unisex rates, when they could obtain annuities in the open market based on sex-specific tables which more accurately reflected their life expectancy. Thus, no insurance company could successfully operate under the plan. Its unisex rates would assume some sort of a "mix" between men and women. But adverse selection would mean that they would, as a practical matter, provide annuities only for women. The consequence would be that insurance companies would no longer be able to offer life annuities under the plan, since they could not afford to provide annuities at unisex rates for women only.[13]

These consequences are certainly undesirable. They are, however, avoidable. A "common sense" and realistic recognition of the *value* of the annuity options offered to similarly situated men and women compels the conclusion that the Arizona Plan provides equality of treatment consistent with Title VII.

II. The Arizona Plan Satisfies *Manhart's* "Open Market" Exception.

In *Manhart*, this Court stated: "Nothing in our holding implies that it would be unlawful for an employer to set aside equal retirement contributions for each employee and let each retiree purchase the largest benefit which his or her accumulated contributions could command in the open market." 435 U.S. at 717-18 (footnote omitted); *see General Electric Co. v. Gilbert*, 429 U.S. 125, 139 n.17. This Court's mention of the

[13] Oddly enough, this consequence would follow primarily because of the "open market" election available under the Plan. To say that the State could not legally offer the open market election would seem to be in the teeth of this Court's decision in the *Manhart* case.

"open market" exception served to allay the concerns of the insurance industry that the reasoning in *Manhart* would disrupt the long-accepted industry practice of using sex-specific mortality tables. The holding in *Manhart* was carefully limited to the facts presented, i.e., an employer-operated pension fund requiring unequal employee contributions. This Court stated: "we do not suggest that . . . [Title VII] was intended to revolutionize the insurance and pension industries." 435 U.S. at 717. Although noting that Title VII applies to an agent of a Title VII employer and that liability could not be avoided by delegating discriminatory programs to corporate shells, this Court stated: "Title VII . . . primarily govern[s] relations between employees and their employer, not between employees and third parties." 435 U.S. at 718 n. 33. The express limitations on the breadth of *Manhart's* holding, including the "open market" exception, indicate that this Court did not intend to extend the reach of Title VII to insurance practices developed and controlled independently of a Title VII employer.

The Arizona Plan in question here falls squarely within *Manhart's* "open market" exception. First, the Arizona Deferred Compensation Plan is voluntary. Therefore, state employees who do not choose to participate may receive all of their compensation in the first instance, and spend these funds or use them to purchase the largest benefit available in the open market. Second, the lump sum option affords an employee who elected to participate in the Plan the opportunity to receive his or her accumulated contributions at retirement. The accumulated contributions, which would of course be identical for similarly situated men and women, would then be available to purchase benefits in the open market.

The court of appeals found that the Arizona Plan fell outside the "open market" exception because the Plan was not limited to concededly nondiscriminatory options. By making available an option (the life annuity) which the court considered discriminatory, the court held that the petitioners violated Title VII. But petitioners merely made available a range of

options which existed in the marketplace. Petitioners made no contributions to the Plan and exercised no supervision over the practices of the insurance companies involved, or over the choices of the employees. As the district court specifically found, petitioners did not exhibit an intent to discriminate: "[the challenged] classification was not made by the defendants but rather . . . [was] the result of the insurers' judgment." 486 F. Supp. at 651.

If annuities were to be among the deferred compensation options (and, apparently, annuities are attractive to many employees, *see* 486 F. Supp. at 647), they would, of necessity, have to be provided by an insurance company which uses sex-specific mortality tables. The Council is not aware of any private insurance company which offers an annuity which does not calculate benefits in accordance with sex-specific actuarial tables. Petitioners are not responsible for the use of such tables; private insurance companies make the decision to use them in order to remain financially sound, as recognized by state insurance regulatory authorities.

The most likely consequence of finding petitioners liable under Title VII for the insurance companies' use of sex-based mortality tables will be to limit the deferred compensation options available to Arizona employees. It would be a strange result if, in the name of equality, all employees were denied the opportunity to purchase annuities of equal value to men and women and of greater value than would be available to each individual employee in the open market.[14] In fact, petitioners

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[14] Professor Kimball has stated:

> With respect, if Justice Stevens seriously meant that the only marketing arrangement his phraseology would accommodate requires accumulation of the funds until retirement and *then* payment over to the retiree who *then* goes out into the world naked and alone to shop for the best bargain in annuities, he stated nonsense. That would have revolutionary effects on portions of the insurance and pension industries, among other ways by depriving employees of the substantial benefits of the mass purchase of group insurance through the employer. It would be very wasteful and it would meet the needs of retired persons much less well. Within the open market notion must be included at least some of the real world ways in which these

(footnote continues)

have (during the pendency of this case) removed the life annuity option from the currently available offerings. This result is neither required by the meaning of discrimination under Title VII nor by an appropriate construction of the "open market" exception. Petitioners, who had no intent to discriminate as required by Title VII, should not be held responsible for the allegedly discriminatory acts of a third party.

The Ninth Circuit asserted that, because no insurance company was a party and because no insurance company had been enjoined, the McCarran-Ferguson Act did not prohibit application of Title VII to the facts presented. According to the court, "the district court has not interfered with the business of insurance." 671 F.2d at 333. But this is too formal an approach. The practical effect of this holding is to prevent insurance companies from using sex-specific tables in employers' pension plans. It is, indeed, an end-run around the McCarran-Ferguson Act. Under the decision, all insurance companies would be barred from doing business with employers on the basis of sound actuarial principles which have been sanctioned by the state regulatory authorities. And this result would be the consequence of the application of a federal statute making no reference to "the business of insurance"—in the teeth of the explicit provision of the McCarran-Ferguson Act.[15]

This holding—even though no insurance company is a party—would revolutionize the insurance and pension industries. Pension plans covering 26.1 million Americans and backed by $165.8 billion in reserves would have to be changed substantially under the Ninth Circuit's decision, with consequences which cannot now be clearly foreseen. The prevention of such an interference with an area that has been

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(footnote continued)

> matters are handled by people dealing at arm's length. The reasonable interpretation is that it includes all of them.

Kimball, *supra*, at 128 (footnote omitted) (emphasis in original).

[15] The McCarran-Ferguson Act question is directly presented by the petition for a writ of certiorari in *Teachers Insurance and Annuity Association v. Spirt* (No. 82-791).

traditionally left to the states was the clearly avowed and stated objective of the McCarran-Ferguson Act. It should not be accomplished by indirect federal regulation.

CONCLUSION

For the reasons set forth above and for the additional reasons advanced in the Brief for the Petitioners, the decision of the United States Court of Appeals for the Ninth Circuit should be reversed.

Respectfully submitted,

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APPENDIX

Aggregate Payments to Men and Women Beneficiaries Under Sex-Specific Mortality Tables

	Age 65		Age 70	
	M	F	M	F
Accumulation at Retirement	$ 10,000	$ 10,000	$ 10,000	$ 10,000
Annuity Factor	85.47629	91.44014	78.10513	85.24887
Monthly Income	$ 116.99(X)	$ 109.36(Y)	$ 128.03(X)	$ 117.30(Y)
Life Expectancy—Months	223.57(A)	263.77(B)	179.54(A)	214.41(B)
Aggregate Sum	$26,155.45(AX)	$28,845.89(BY)	$22,986.51(AX)	$25,150.29(BY)
BY—AX	$2,690.44		$2,163.78	

Assumptions: Annuity Factor based on 1983 Table "a" with interest at 12%.

Life Expectancy based on 1983 Table "a".

1983 Table "a" was adopted by the National Association of Insurance Commissioners in June, 1982.